II. EXECUTIVE SUMMARY

The Project was a large, complex, multi-faceted real estate development which, for purposes of our review, spanned approximately three years. The SDAG's report on the matters within the scope of work for which we are primarily responsible is over 430 pages, including the appendices. It is therefore extremely difficult, if not impossible, to adequately summarize what we believe occurred in the Project. The following summary is therefore not intended to take the place of the full report, and the reader must review the report in its entirety in order to better understand the information we relied upon and the analysis we undertook in reaching the observations and the conclusions included in this executive summary.[4]

A number of troubling and serious issues emerged from the review of the Project. These issues include those related to internal controls, disclosures, culture, conflicts of interest, use of funds, and vision and enthusiasm that at times displaced caution. Our observations and conclusions, which are discussed more fully in the remainder of the report, can be summarized as follows:[5]

A. PROJECT VISION

One of the UI's principal goals in its Strategic Plan is to "Expand the capacity and delivery of outreach programs and services in keeping with the University of Idaho's land-grant mission." The UI has provided programs in the Boise area for over 75 years. In the late 1990s the UI, led by President Hoover, explored not only consolidating the then existing programs it was offering in the Boise area at one location, but to also expand the number of programs being offered. To that end, UI engaged consultants to assist it in locating a suitable site, and it conducted studies that indicated a need for the delivery of additional educational services in Boise. The UI quickly focused on downtown Boise and, at the request of the UI, in January of 2000 the UIF acquired 2.51 acres of land bordered by Broadway, Front and Myrtle Streets.

This property, which is located just north of Boise State University, was intended to be the cornerstone for the UI's planned expansion of its presence in Boise. This plan became known as the UniversityPlace/IWC Project. The UI contemplated that the Project would provide space for the UI, Idaho State University, state and federal agencies and private entities. The plan for the Project evolved into what was hoped to be the initial construction of four buildings with a total of approximately 500,000 square feet of space together with parking and sites for additional buildings in the future, all located on approximately 7.8 acres. In short, it was to be a large, complex

[4] A summary of KPMG's findings are included in Part 2 of this report and will not be repeated here.

[5] A summary of KPMG's findings are included in Part 2 of this report and will not be repeated here.

project, one which neither the UI nor the UIF had ever before attempted, and one which neither the UI nor the UIF had the available personnel to adequately manage and complete. We found comments from project leaders early in the Project about its scope and size, stating that the buildings should "be as tall and as large as they can be." The size of the Project, including the expansion space, was intended to provide the UI with a large, highly visible academic presence in Boise that would not only serve the UI's present needs, but also satisfy anticipated space requirements for the UI's planned future expansion.

B. UIF BOARD VOLUNTEERS

It is important to remember that the UIF Board is comprised of volunteers. The number of hours each board member spends on UIF matters will, by necessity, vary because typical board members have successful businesses and careers of their own to manage. The board members collectively spend hundreds of volunteer hours for the betterment of the UI because of their love for the institution. That dedication and devotion to the UI appears, however, to have significantly contributed to the UIF leadership's exercise of questionable business judgment in committing UIF and trust assets to the Project. Though UIF Board members raised a few questions about the Project along the way, in the end it appears that what the UI, and in particular President Hoover, wanted by way of financial support for the Project, was received. After all, the UIF was then about to conclude, before its scheduled date, a capital campaign which began in 1998 and raised over $110 million. This process and culture may best be summarized by comments we heard to the effect that if you questioned the Project you were not a loyal Vandal, and that if President Hoover wanted it, the Foundation's job was to deliver it.

C. PROJECT LEADERS

UniversityPlace/IWC Project was a large, complex, multi-faceted real estate development. As a result, numerous people worked on various aspects of the Project but, in our opinion, the driving forces behind the Project were, for the UI, President Hoover and Jerry Wallace and, for the UIF, Roy Eiguren and Pat McMurray.

The UIF Board formed a committee known as the Property Development Committee (PDC), which was charged with the responsibility of overseeing the Project on behalf of the UIF. Though the PDC did not have authority to bind the UIF, its recommendations were uniformly adopted by the UIF Board, and we found that the UIF Board heavily relied upon the PDC. McMurray and Eiguren were the co-chairs of the PDC and the committee consisted of five people. Eiguren and McMurray were, in our opinion, the only members of the PDC who were actively engaged in the Project. As a result, the recommendations to the UIF Board from the PDC were typically the recommendations of Eiguren and McMurray. Hoover and Wallace's roles in the Project are more specifically addressed in the next section.

D. PRESIDENT HOOVER'S LEADERSHIP

At the outset, it is important to remember that President Hoover had many significant accomplishments during his tenure at UI. In some ways, however, those accomplishments contributed to the failure of the Project. Namely, even though millions of dollars were being spent on pre-construction costs without any ensured source of repayment, many with whom we spoke believed that Hoover and Eiguren formed a "dream team" that could "make it happen."

In this report there are numerous references to actions and decisions taken either by Jerry Wallace or at his direction. This is because President Hoover selected Wallace to manage the project and be the UI's "point person." As a result, the references to Hoover in the report are not as numerous as those to Wallace. It is, however, clear to us that the Project's vision, including its size and complexity, was Hoover's. Wallace ardently supported this vision, and Hoover empowered and directed Wallace to turn Hoover's vision into reality at an accelerated pace. There was, in our opinion, a significant amount of pressure to complete the Project while Hoover was President of the UI, and this resulted in the need to quickly move the Project to completion. This was the genesis of the often-repeated phrase "Hoover time," which meant that everyone must work at an accelerated pace to assure that the Project was completed by a certain date. At times, the pressure of "Hoover time" resulted, in our opinion, in the UI and UIF taking improvident risks in an effort to deliver the Project on time. An example of this was in April 2001 when President Hoover was faced with the decision of whether to hold the Project in place until the legislature approved the issuance of the ISBA Bonds in the following legislative session (and thereby not spend millions of dollars on it) or to proceed full-speed ahead without permanent financing in place in order to meet the self-imposed construction deadline. President Hoover elected to proceed, and this resulted in the expenditure of over $26 million, much of which will likely never be recovered.

The UI's Executive Council, a group of UI leaders led by Provost Pitcher, was charged with the responsibility of reviewing major policy decisions prior to submitting them to Hoover for approval. The Executive Council did not, however, function in that capacity on the Project. Rather than vetting issues and concerns in a group setting and obtaining input from the full leadership team, individuals, and in particular Wallace, often met with Hoover one-on-one. As a result, the members of the Executive Council thought the group forum became a waste of time since decisions were being made without their input. To make matters worse, it appears that if someone raised a question about or an objection to the Project they were excluded from future participation in the Project. Further, Wallace's personal dynamics appear to have exacerbated the breakdown of communications within the UI. It was reported to us that his temper and efforts to intimidate stifled critical analysis of the Project and resulted in subordinates not being able to report their concerns about the Project without the fear of retribution. One person in particular affected by this was Harris, who was directed by Wallace to perform many of the actions addressed in this report. Consequently, we believe the UI should implement a system by which employees are able to report questionable actions by their superiors without the fear of retribution.

E. PROJECT INTERIM FINANCING

Interim financing for the Project was provided by the UI and the UIF. These funds originated from four primary transactions totaling $27.6 million in principal debt for the UIF:

1. $1,900,000 loan from the UI's cash management fund in January 2000 to enable the UIF's purchase of the Rite-Aid Parcel.

2. $8,059,122.68 in net spending between November 2000 and January 2003 from the UI's cash management fund through an alleged agency account.

3. $12,000,000 loan from the CIT authorized by the UIF in April 2001.

4. $5,700,000 promissory note issued by the UIF to Civic Partners in conjunction with the Reconciliation Agreement in July 2002. In order to pay this note in January 2003 the UIF borrowed $6 million from UBS Paine Webber secured by both restricted and unrestricted, non-CIT assets in UIF's Paine Webber account.

Our conclusions with respect to each of these transactions are set forth below.

1. Rite-Aid Loan

UI requested that the UIF purchase the Rite-Aid property. To enable this purchase, the UI loaned the UIF $1.9 million. The funds from this loan came from the UI's cash management general ledger (account #990151). Wallace received a legal memorandum from Hawley Troxell, which concluded that there were no express provisions in either Idaho law or the SBOE's policies regarding the UI's authority to loan the UIF funds for the purpose of purchasing real property, but that the UI was required to report the loan/investment to the SBOE (the "Hawley Memo").

Wallace consistently characterized this transaction in conversations with him as an investment, and not a loan, of UI funds. We believe, however, that the transaction should be more properly characterized as a loan. We also believe that the SBOE policies governing spending UI funds would have likely required prior SBOE approval of the transaction, irrespective of whether it was classified as a loan or an investment. The UI did not obtain either prior to or after the fact approval from the SBOE for this use of UI funds. The loan was also not ever expressly disclosed to the SBOE, other than in a footnote to the UI's FY 2000 audited financial statements, which refers to a promissory note.

Having said this, we believe it was reasonable for Wallace, Hoover, and the other UI leadership to rely on the advice in the Hawley Memo that there was no prohibition against lending university funds to the UIF, a conclusion with which we disagree. The Hawley Memo cannot, however, be relied upon to explain their failure to properly disclose the loan to the SBOE.

2. Agency Account

Between November 2000 and January 2003, the UI spent approximately $8 million from the purported UIF agency account. Wallace directed his staff to create the agency account in November 2000, and as of June 2001 had spent approximately $2.2 million. By June 2002, the balance grew to nearly $6.1 million, and by January 2003 the balance reached just over $8 million.

An agency account is designed to work as follows: an organization deposits funds with the UI, and the funds are included in the UI's cash-management system in order to maximize income. When the organization needs money it withdraws funds from its account. The UIF, however, never deposited any funds into the agency account and, as a result, it always carried a deficit balance. Indeed, many UIF Board members stated to us they did not know that the agency account existed until January 2003. Laura Hubbard best explained an agency account when she said it was supposed to act as a debit card, and not a charge card. Wallace and the UI, however, treated the agency account as a charge card.

During his interview, Wallace stated that he relied on the Hawley Memo to justify his treatment of the agency account as an authorized investment of UI's surplus cash. Our analysis of this is as follows:

(i) We do not believe the use of the agency account can properly be characterized as either a loan to the UIF or an investment of UI's surplus funds. It was, in our opinion, an unauthorized use of UI funds.

(ii) We do not believe it was reasonable for either Wallace or other UI leaders to have relied on the Hawley Memo to justify their use of the agency account. Further, the UI did not expressly disclose to the SBOE its use of the agency account. The only disclosure came after the amounts had been expended and the deficit account converted to a promissory note signed by the UIF. This note obligation was referenced in a footnote contained in the UI's FY 2002 audited financial statements.

(iii) We believe that irrespective of how the use of the agency account is characterized, its use by the UI violated SBOE policies and possibly state law.

3. CIT Loans

In April 2001, the UIF took the following actions. First, it amended its CIT investment policy by raising the maximum asset allocation to alternative and real estate investments from 5% to 10%. Second, it passed a resolution that authorized the UIF investment manager to loan the UIF up to $13.9 million of CIT funds for the purpose of covering Project expenses until a source of permanent financing was in place. Subsequently, $12 million of CIT funds was loaned to the UIF.

The CIT is not by itself a single trust. It is instead comprised of assets from numerous individual endowments, which are pooled for investment purposes. Each endowment is issued unit participation shares in the investment account called the CIT. As a result, the profits and losses on the investments are shared among the individual endowments based on the percentage each endowment has of the total assets in the pooled investment account. The UIF is a trustee of these assets and, as a result, has fiduciary duties in respect of the endowment assets.

Based on our review of the propriety of the UIF's loan of CIT trust funds to itself for the purpose of financing a UIF real estate project, we believe there are serious questions with regard to whether the UIF acted properly in regard to this self-dealing. Based on our research, we believe:

(i) **Likely Breach of Fiduciary Duty of Loyalty**. There is a strong likelihood that the UIF breached its duty of loyalty when it made a loan of CIT trust funds to itself for the purpose of financing its own real estate development. The UIF's decision to increase the maximum allocation to alternative and real estate investments for the purpose of providing interim financing for the Project also may have been a breach of the UIF's duty of loyalty.

(ii) **Possible Breach of the Fiduciary Duty of Care**. There are a number of facts that suggest the UIF breached its fiduciary duty of care as a trustee by loaning CIT trust funds to itself as a short-term "alternative investment."

We also have the following additional concerns in regard to the UIF's management of the CIT:

(a) **UIF Financial Statements**. The UIF authorized the use of $13.9 million in CIT funds in April 2001. The first $10 million was loaned to the UIF under the terms of an Investment Deposit and Disbursement Agreement dated July 1, 2001 (Disbursement Agreement). The Disbursement Agreement required the $10 million to be repaid on or before June 30, 2002. Between April and July 2001, the Project's costs were paid out of the UI's agency account. The UI and UIF's fiscal years began on July 1 and ended on June 30.

We were told during our interviews that the reason for delaying the use of the CIT funds until July 1, 2001, was that it took until July 1, 2001 to liquidate sufficient investments to fund the loan to the UIF and that the reason for choosing the June 30, 2002, due date for the loan was that they were told it would only take six or seven months for permanent financing to be in place, so a few extra months was allowed in the event there was a delay.

We, however, found evidence that suggests an intent that the loan be made and paid within the same fiscal year so that it would not be disclosed in the UIF's audited financial statements. If this occurred, no one other than the UIF Board members and UI leaders would know about the UIF's use of CIT trust assets to fund its own real estate project.

(b) **Failure To Disclose**. We do not believe the use of CIT assets to fund the Project was adequately disclosed to the SBOE. This is addressed in Section III. M. below.

4. UBS Paine Webber

As part of its termination with Civic Partners, the UIF agreed to pay Civic Partners $5.7 million when the ISBA bonds were issued. Since the UIF did not receive any reimbursement for its pre-construction costs at the time the bonds were issued, the UIF was faced with finding another source of funds to pay Civic Partners. The UIF again turned to the assets it held in trust. This time it was the assets held in the UIF's account with Paine Webber. We were told during our interviews there were no CIT assets in the Paine Webber account. Approximately 90% of these assets were, however, restricted in the sense that various donors had made gifts with the condition that the UIF use the funds for a specific purpose. The UIF Board decided on January 8, 2003, to borrow up to $6 million from UBS Paine Webber (an investment bank affiliated with Paine Webber) and to secure this loan with trust assets held in the Paine Webber account.

We reviewed the propriety of the UIF using restricted trust assets to secure the UBS Paine Webber loan to the UIF. Based on that review, we believe there are serious questions with regard to whether the UIF acted properly. As a result of our research, we believe:

(1) **Likely Breach of the Fiduciary Duty of Loyalty**. We believe there is a strong likelihood that the UIF breached its duty of loyalty when it pledged the trust funds as collateral in order to secure a loan to the UIF for the purpose of paying amounts due on the UIF's own real estate project.

(2) **Possible Breach of the Fiduciary Duty of Care.** There is a strong suggestion that the UIF also breached its duty of care when it pledged the trust funds as collateral. Because there was no return to be gained from pledging the trust funds as collateral to secure the UIF's loan, the UIF may have not adequately addressed the risk and return objectives for these trust assets, as required by state law.

F. CIVIC PARTNERS

The UIF and UI's decision to move the IWC into the Ada County Courthouse Corridor Project had a major impact on the Project. This move significantly increased the complexity and cost of the Project. Further, after it was determined that the ISBA would provide the permanent financing for the IWC, the UIF elected to terminate its relationship with Civic Partners. We find it troubling that Civic Partners was retained by UIF without the UIF requesting proposals from other parties; that a development agreement was never entered into between UIF and Civic Partners; and that Civic Partners appears to have been able to dictate the terms upon which the relationship between UIF and Civic Partners was terminated, even though nothing more than a memorandum of understanding existed between the parties.

We are also troubled by the fact that Civic Partners needed $5.7 million to close its adjacent housing project and that the UIF agreed to pay Civic Partners exactly that amount. Further, even ignoring the parking and infrastructure contribution paid by UIF to Civic Partners in the amount of $2.5 million, $5.9 million was paid for the IWC site.[6] We question whether the IWC condominium site is worth $5.9 million when the UIF paid $1.9 million for the Rite-Aid Parcel across the street, especially when the two parcels are approximately the same size.

G. LEGAL CONFLICTS OF INTEREST

The UIF was represented by two law firms with regard to the Project, Givens Pursley and Elam & Burke. Givens Pursley was retained in 1999 to explore possible purchases of property in the Boise area for the UI. Through the course of the Project, Givens Pursley came to represent the UIF, and possibly the UI, in a role referred to as "Special Project Counsel." Givens Pursley provided the UIF (and in one case the UI) with four separate conflict of interest letters, requesting waiver of its potential conflict of interest in its representation of the UIF and/or UI along with its former or current representation of the following parties: Thrifty Payless, Inc., Cantlon Properties, Inc., and Civic Partners.

---

[6] The UIF paid Civic Partners approximately $4 million (including the $2,060,000 relocation cost), plus $1.9 million was paid to Ada County for the present value of the ground rent.

Elam & Burke represented the UIF as general counsel. In late 1999, Elam & Burke began providing legal services related to the acquisition and financing of the Rite-Aid property. Thereafter Elam & Burke represented UIF on other aspects of the Project. Elam & Burke provided the UIF with two conflict letters pertaining to its representation of CCDC.

The UIF refused to waive its attorney-client privilege with regard to Elam & Burke and, as a result, we were unable to speak to Ryan Armbruster. The UIF waived its attorney-client privilege with regard to Givens Pursley, and we therefore talked to Ed Miller and Frank Lee. Our inability to talk to Armbruster significantly hindered our ability to review the facts and issues related to Givens Pursley and Elam & Burke's representation of UIF and other parties who were actively involved in the Project. Specifically, though we were able to review various documents, it was difficult to determine the exact roles Elam & Burke and Givens Pursley played in the Project, especially in relation to Civic Partners and CCDC. Because of this, our observations concerning the legal conflicts of interest of these firms are, by necessity, preliminary in nature. As with other topics in this Executive Summary, the reader must review the report in its entirety (and in particular, Sections III. G and V. as to this topic) in order to better understand the information we relied on and the analysis we undertook.

We believe Givens Pursley's representation of the UIF and/or UI, Thrifty Payless, Inc., Cantlon Properties, Inc., and Civic Partners raises the issues set forth below. Our initial observations on these issues are as follows:

(1) whether Givens Pursley properly addressed its potential conflict of interest in the UIF's acquisition of the Rite-Aid property

It appears that Givens Pursley properly handled its representation of UI, UIF, and CPI in this transaction.

(2) whether Givens Pursley failed to properly address a potential conflict of interest in representing both the UIF and the UI

We found that there was some confusion over whether Givens Pursley was solely representing UIF or whether it was also representing UI on the Project. Irrespective of whether Givens Pursley was representing both the UIF and the UI, we believe there are questions as to whether Givens Pursley properly addressed the potential conflicts of interest between UI and UIF.

(3) whether Givens Pursley properly addressed its potential conflicts of interest in providing legal services to both Civic Partners and the UIF.

Givens Pursley has consistently taken the position that it did not act as an advocate for either UIF or Civic Partners in their negotiations, but instead limited its role to that of raising issues and drafting documents. Givens

Pursley stated that Elam & Burke acted as the advocate during negotiations with Civic Partners. Elam & Burke's conflict letters to the UIF, however, state that Givens Pursley would act as the advocate for the UIF "in connection with the numerous transactions relating to the Water Center and Idaho Place," "that Elam & Burke's role will be limited to compliance with general corporate statutory article and bylaw provisions as opposed to substantive business points" and that it "will not be an advocate of the Foundation in connection with the actual formation and negotiation of business terms and in the drafting of the documentation." In addition to Givens Pursley's representation of the UIF and Civic Partners, Roy Eiguren was a: (i) UIF Board Director, (ii) lobbyist for the UI and UIF, and (iii) partner at Givens Pursley.

As discussed in Section III. G and V., we question whether Givens Pursley properly addressed the potential conflicts of interest between UIF and Civic Partners.

Elam & Burke's representation of the UIF and CCDC also raises the question of whether Elam & Burke properly addressed its potential conflict of interest with the UIF. A Givens Pursley conflict letter stated that Elam & Burke would represent UIF in negotiations with Civic Partners, and Elam & Burke's conflicts letter stated, among other things, that Elam & Burke would not represent the UIF on various matters, including "any transaction or agreement which may involve CCDC." In addition, Elam & Burke stated in the conflict letter that it "may represent and advocate the position of CCDC." The Reconciliation Agreement with Civic Partners included a number of CCDC-related issues, such as termination of the existing sublease and parking contributions. As noted before, we were not allowed to interview Ryan Armbruster of Elam & Burke. There are therefore unanswered questions concerning whether Elam & Burke properly addressed this conflict of interest issue with UIF.

H. Operating Budget Issues

The UI manages an annual operating budget of approximately $285 million, with only approximately one-third coming from state-appropriated funds. The UI receives the remaining two-thirds from such sources as tuition, student fees, auxiliary revenues (such as athletics and the bookstore), research grants and contracts, forestry operations, gifts, and other similar sources. During the fall of 2001, the UI was facing a 10 percent reduction in appropriated funds and a further cutback in expenses. At this same time the UI was developing its FY03 budget, and during that process discovered that the UI was facing a $30 million shortfall. A plan was developed to address most of this shortfall, but a notable piece of information was missing—the operating budget for the Project was consistently noted as "TBD" (to be determined).

This unknown variable greatly concerned Wayland Winstead and prompted his consistent requests to Wallace for operating cost estimates. Ken Harris and Laura

Hubbard met with Winstead in early February 2002 and provided him with their estimate of the operating costs for the Project. Winstead's response is now well known. He wrote a series of memoranda in which he outlined the grave financial risks that confronted the UI on the Project and, in addition, pointed to the significant one-time expenses the UI would be required to pay.

Winstead's memorandum raised many of the issues that caused the UI in 2003 to not go forward with the Project, beyond construction of the IWC. At the risk of stating the obvious, operational costs are an extremely important component to any capital project and need to be thoroughly analyzed and understood before proceeding with a capital project. The Project's capital costs (the costs to plan and construct it) were not, in our opinion, adequately understood or controlled by the UI, and inadequate attention was paid to the Project's operational costs.

I. ISBA

The UIF and UI's plan for the Project's permanent financing was initially based on what they referred to as "conduit financing." In this role, the UIF was to provide tax-exempt financing for the UI and its collaborative partners. This, however, was eventually abandoned because the tax regulations required that the UIF could only act on behalf of the UI. Given the intended participation of ISU, IDWR, and the United States Forest Service, this was a major hurdle. As a result, the UIF and UI turned to the ISBA as a way to obtain permanent financing for the IWC and UniversityPlace.

Many UIF Board members and UI leaders blamed the ISBA for the delay in closing the IWC bonds and for UIF receiving no reimbursement for its pre-construction costs at the time bonds were issued. In our opinion, this blame is largely misplaced because: (1) the ISBA raised the issues which were required to be resolved early in the process, and those issues had, for the most part, to be resolved by the UIF and UI; and (2) the ISBA's ability to reimburse the UIF was constrained by the amount approved in the concurrent resolution adopted by the state legislature (and it was the UIF and UI that prepared the budget for the legislature). ISBA was required to assure that there were sufficient funds with which to construct the IWC before there could be any prospect of the UIF being reimbursed. ISBA's consultants believed that the entire budgeted amount was potentially needed to construct the IWC. As a result, any reimbursement the UIF would receive had to come after the ISBA was confident there were in fact sufficient funds to construct the IWC.

J. UI'S RELATIONSHIP WITH SBOE

It appears UIF's anticipated ownership of the Project (and the UI's support of this) was motivated in part by a desire to: (1) prevent the SBOE from being able to transfer the property to another university in the future; (2) make it more difficult for the SBOE to control the use of the property; and (3) avoid reporting to and obtaining interim project funding approvals from the SBOE, which would have been required if it was a UI project.

We also found what appeared to be an adversarial relationship between the UI and the SBOE. It was reported that UI leaders were suspicious of whether the SBOE's true motivation in raising questions about the viability of the Project was an effort to ensure that the Project did not succeed. This could possibly have been a result of what was described to us as the "Vandal effect," namely the culture of "if you are not with us, you must be against us." This may have had a number of different impacts on the Project, including the decision to place it on a fast track and the UI's advocacy before and failure to fully disclose all of the risks to the legislature and the SBOE.

Another cultural aspect reported to us as having impacted the Project was the belief that when a problem arose in the Project, it could be resolved "Vandal to Vandal." At times when a problem was encountered with the Project, the response was not to address the issue directly but to instead determine who could be "talked to," especially if that person had ties to the UI. Even though this approach was taken on occasion, it does not appear it was consistently successful, especially as it related to the ISBA.

K. DISCLOSURE

Our research revealed no law mandating full and open disclosure when testifying before the legislature or a state agency. In fact, the perjury laws do not apply unless the legislature exercises its option to require that testimony be given under oath.

We did <u>not</u> find that there was false testimony before the legislature concerning the Project. Namely, what was said in the hearing of which we had a transcript was technically correct. We, however, believe that relevant, material information was omitted from the testimony. Examples of this include the testimony to the effect that the ISBA, and not the state, would repay the bonds (and thus there is "no risk to the state"). There was not, however, an explanation of the impact to the state that the UI's failure to renew its annual lease and a subsequent default on the ISBA bonds would have on the state's credit rating and on its future cost of funds (i.e., the resulting potential increased interest rate on future bond issuances). There was also testimony to the effect that tenant agreements would be in place before the bonds closed, and financial viability due diligence would be completed when the ISBA only required the UI to sign the master lease, without any subleases being in place. Reference is made to Sections III. K and VI. A. for a full discussion of the adequacy of the disclosure to the legislature.

We believe that the UI had a fiduciary duty to disclose all relevant, material information to the SBOE. Though we found no state statute that concerns disclosures to a state agency, we believe that officers of UI, as agents of the SBOE, owe fiduciary duties to the SBOE, including the duty to fully disclose relevant, material information needed by the SBOE to make an informed decision. This duty requires more than merely avoiding false information, it requires UI employees to fully communicate material, relevant information; even if the precise question is not asked. We believe UI officials breached this duty by, in some instances, providing misleading information to the SBOE and in not fully disclosing material, relevant information. When responding to written questions and testifying before the SBOE, it appeared to us that the UI officials carefully chose their words and only responded to the precise question posed, nothing more and in some instances their responses were misleading.

Reference is made to Sections III. M. and VI. for a full discussion of the adequacy of the disclosures before the SBOE. By way of illustration we believe:

a. The UI did not disclose the cost overrun/UIF reimbursement problem that had grown significantly by December 2002 and was exacerbated by the Civic Partners termination.

b. In spite of the zero UIF reimbursement, the UI did not disclose either the lack of reimbursement or, more importantly, the loans from the UI and the CIT totaling $13.9 million and the approximately $8 million spent through the agency account.

c. Although the UI lowered its occupancy assumption from 100% to 50% in December 2002, it still did not have any tenants secured other than IDWR. As the SBOE feared in June, the ISBA accepted the UI's master lease on the IWC and allowed the bonds to close without any further commitments from tenants.

d. There was no disclosure of the requirement to pay Civic Partners at the closing of the bonds and of the resulting impact that would have on the UIF's financial condition.

There was also testimony by non-UI-employees, especially in the June 2002 SBOE meeting, to the effect that there was "no risk to the state or the university" in the transaction and that the ISBA would perform extensive financial due diligence in order to satisfy itself that the Project was financially viable before issuing the bonds. This testimony was similar to the testimony before the Legislature and, as with the Legislature, we believe the same material, relevant information, was omitted.

L. COSTS OF THE PROJECT

KPMG, in its report, analyzes the Project's pre-construction costs, including land acquisition and interest expense. KPMG's analysis was, of course, based on available Project documentation and showed a cost of $32,782,880, exclusive of operational costs. We, however, have found evidence of additional expenses being incurred in regard to the Project that were not included in the costs paid by the UIF or thorough the UI's agency account. For example, on July 24, 2002, Glenn Wilde wrote an e-mail to Larry Brannen in which Wilde said that during the prior year IdahoPlace travel and communication costs for the IT staff had been allocated to the "Outreach/Technology" budget, but that in light of the budget cuts these expenses could not continue to be allocated in that manner. Wilde estimated the costs at $10,000. In a reply e-mail later the same day, Wilde said, "These are the "hidden" costs outside the $30 million already expended that really add up as part of the total institutional costs in support of that development." There are likely other instances where costs related to the Project were paid from a department's own budget. In addition, an enormous amount of time was devoted to the Project by numerous UI employees. Further, interest continues to accrue on the approximate $25,300,000 in remaining UIF debt, the amount of the debt as of September 30, 2003, as set forth in KPMG's report.

In addition to the pre-construction costs, there are, of course, operational expenses that the UI will be required to pay. These costs include the one-time move-in costs, salaries, and related expenses. The UI will also be faced with paying its allocated portion of the bonds issued to construct the IWC. The IWC bonds were divided into taxable bonds of $17,070,000 and tax-exempt bonds of $37,655,000, for a total of $54,725,000, the amount necessary to fund the estimated $48,000,000 of Project costs, the capitalized interest during construction, and the bond issuance costs.

HCR 60 provided for the IWC bonds to have a thirty-year term. The taxable bonds were issued with a term of twenty-six years (final payment due September 1, 2029), and the tax-exempt bonds were issued for a forty-year term (final payment due September 1, 2043), and a call at par after ten years. The additional ten-year term of the tax-exempt bonds was justified to the 2003 legislature by the representation that the "average life" of the bond issues is 29.662 years.[7] The forty-year term of the tax-exempt bonds "was necessary to meet the University's annual lease rate requirements."[8] The debt service was "back loaded" and structured to begin with payments of no more than $2.9 million through fiscal year 2010 and increasing to $3.7 million per year in 2021-2043. This, of course, results in significant additional interest expense being paid by the UI to service the $37,655,000 debt (the 40-year Bond) for ten additional years and, just as important, requires a future UI administration to pay substantially more per year in payments than the initial payments.

The total cost of the Project may never be known with certainty. One thing is certain, however, the Project will fiscally impact both the UI and the UIF for many years to come.

---

[7] Idaho State Building Authority, Summary of Bond Sizing and Term, 2/21/03, presented to the Joint Finance-Appropriations Committee on February 25, 2003.

[8] Idaho State Building Authority, Summary of Bond Sizing and Term, 2/21/03, presented to the Joint Finance-Appropriations Committee on February 25, 2003.